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No. 917

In the Supreme Court of the United States

OCTOBER TERM, 1960

ANDREW M. SPHEERIS AND ISMENE A. SPHEERIS,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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OPINIONS BELOW

The memorandum findings of fact and the opinion of the Tax Court (R. 2–14)[1] are not officially reported. The opinion of the court of appeals (Pet. 1a–6a) is reported at 284 F. 2d 928.

JURISDICTION

The judgment of the court below was entered on December 13, 1960 (Pet. 7a), and the order denying the petition for rehearing was entered on January 25, 1961 (Pet. 8a). The petition for a writ of

[1] Record references are to the appendix to the petitioners' brief in the court of appeals which has been filed as a part of the record in this Court.

certiorari was filed on April 21, 1961. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the record supports the holdings of both courts below that payments which Andrew Spheeris received from a corporation which he and his relatives controlled were not loans but were taxable as dividends.

STATUTES INVOLVED

Internal Revenue Code of 1939:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * *, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * *
>
> (26 U.S.C. (1952 ed.) 22)
>
> SEC 115. DISTRIBUTIONS BY CORPORATIONS.
>
> (a) *Definition of Dividend.*—The term "dividend" when used in this chapter * * * means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable

year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made. * * *

* * * * *

(26 U.S.C. (1952 ed.) 115)

Internal Revenue Code of 1954:

SEC. 61. GROSS INCOME DEFINED.

(a) *General Definition.*—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

* * * * *

(7) Dividends;

* * * * *

(26 U.S.C. 61)

SEC. 316. DIVIDEND DEFINED.

(a) *General Rule.*—For purposes of this subtitle, the term "dividend" means any distribution of property made by a corporation to its shareholders—

(1) out of its earnings and profits accumulated after February 28, 1913, or

(2) out of its earnings and profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

Except as otherwise provided in this subtitle, every distribution is made out of earnings and

> **profits to the extent thereof, and from the most recently accumulated earnings and profits. To the extent that any distribution is, under any provision of this subchapter, treated as a distribution of property to which section 301 applies, such distribution shall be treated as a distribution of property for purposes of this subsection.**
>
> * * * * *
>
> (26 U.S.C. 316)

STATEMENT

The relevant facts, as found by the Tax Court (R. 3–9) and by the court of appeals (Pet. 1a–6a), may be summarized as follows:

Petitioner,[1] in early 1946, participated in the organization of the Miller Theater Corporation. The authorized capital stock of 500 shares was divided equally among petitioner and his brothers-in-law, C. J. Papas and S. J. Papas. The success of the corporation's theater business depended upon obtaining first-run pictures, and negotiations were conducted with United Artists Corporation, which led to three contracts dated June 11, 1946. Under the first agreement, the Miller Theater Corporation was reorganized and its name was changed to Milwaukee Towne Corporation (hereinafter referred to as Towne); the capital stock was changed to 400 shares of class A stock which were to be purchased by petitioner and

[1] Andrew M. Spheeris and Ismene A. Spheeris, his wife, filed joint income tax returns for the calendar years involved, 1953, 1954, and 1955 (R. 3). The wife is a party by reason of the joint return. For convenience, Andrew M. Spheeris will be referred to as "petitioner."

his two brothers-in-law, the original stockholders of Miller Theater Corporation, and 200 shares of class B stock which were to be purchased by United Artists; and all the stockholders were to make loans to Towne (R. 3–4; Pet. 2a). Since 1946 the ownership of all 400 shares of class A stock, except for 48 shares held in trust for United Artists, has been in the hands of petitioner and his family,[1] who have operated Towne as a close family unit, without even a meeting of the board of directors or stockholders of Towne since September 3, 1948 (R. 5, Pet. 3a).

Towne received loans in substantial amounts during the years 1946 through 1949 from petitioner, from his father-in-law, John Papas, from United Artists, and from corporations owned or controlled by members of the Spheeris and Papas families. All the loans, which were repaid by April 30, 1952, were evidenced by promissory notes issued in favor of the prospective lenders, bearing interest of four percent per annum, which interest was in fact paid (R. 5–6; Pet. 3a).

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[1] The authorized capital stock of Towne has been held since November 1946, as follows (R. 4–5; Pet. 3a):

Name.	Class	No. of shares
A. M. Spheeris	A	117 34/100
Mary J. Papas	A	77 33/100
C. J. Papas	A	78 33/100
S. J. Papas	A	78 33/100
John Papas	A	1
B. C. Dolar, Trustee	A	48
United Artists	B	198
Edward Raftery	B	1
Rud. Lohrens	B	1
Paul Lazarus, Jr.	B	1
Ralph Cramblett	B	1

In 1952, Towne received an award of approximately $1,000,000 as treble damages in an antitrust action which had been brought against various companies in the film industry. *Milwaukee Towne Corp.* v. *Loew's, Inc.*, 190 F. 2d 561 (C.A. 7). In 1954, Towne received approximately $300,000 in settlement of another such case (R. 6, Pet. 4a). From 1952 to 1956 the accounting records of Towne reflected a reserve for contingencies in the amount of $550,000 and a substantial earned surplus, amounting in 1956 to $208,589.65 (R. 6–7).

Beginning in 1953 and through the years in issue, petitioner and other stockholder-members of his family withdrew funds from Towne for personal use. The dates and amounts of petitioner's withdrawals of Towne's funds, as reflected in an account in petitioner's name and as carried on Towne's books, are as follows (R. 7–8; Pet. 3a–4a):

Date	Debit	Credit	Debit balance
May 27, 1953	$5,000.00	$	$5,000.00
Sept. 30, 1953	15,000.00		20,000.00
Oct. 28, 1953	16,500.00		36,500.00
Mar. 31, 1954	5,000.00		41,500.00
Apr. 28, 1954		[4] 23,547.27	17,952.73
Apr. 28, 1954	25,000.00		42,952.73
Mar. 30, 1955	9,000.00		51,952.73
Apr. 27, 1955	5,000.00		56,952.73
May 24, 1955	3,000.00		59,952.73
Oct. 31, 1955	2,500.00		62,452.73
May 23, 1956		5,000.00	57,452.73
Nov. 30, 1957	1,500.00		58,952.73

[4] The $23,547.27 credit listed is a bookkeeping transaction and does not report a cash payment. It was simply a transfer of the credit from the account of the estate of C. J. Papas to petitioner's account. On the same day that the credit was passed to petitioner's account he withdrew an additional $25,000. The only other credit reducing petitioner's account was a $5,000 entry on May 23, 1956, which was subsequent to the time that petitioner was apprised that the Internal Revenue audit, upon which the determinations under consideration are based, had begun (R. 8).

Corporations with which petitioner and members of his family were closely associated and in which they held controlling interests also received funds from Towne during this period. No withdrawals were made on behalf of United Artists (R. 7; Pet. 3a).

The withdrawals were entered in the books of account of Towne as "Accounts Receivable-Miscellaneous." None of the withdrawals were evidenced by promissory notes or secured by any other form of collateral. There was no provision made for payment of interest to Towne and, in fact, no interest was ever paid. No date of repayment was agreed upon (R. 7; Pet. 3a–4a). Towne formally declared no dividends during this period (R. 9; Pet. 4a).

The Tax Court found that the withdrawals made by petitioner from Towne in 1953, 1954, and 1955 were out of earnings and profits of Towne accumulated after February 28, 1913, and were dividends as defined in Section 115(a) of the Internal Revenue Code of 1939, and Section 316(a) of the Internal Revenue Code of 1954 (R. 9, 14). The court of appeals held that the Tax Court was correct in concluding that the legal effect of the payments was to provide dividends to petitioner (Pet. 5a–6a).

ARGUMENT

The Internal Revenue Code provides, in general, that any distribution made by a corporation to its stockholders out of the corporation's earnings and profits accumulated after February 28, 1913, or out of earnings or profits of the taxable year constitutes an ordinary dividend which is includible in the re-

cipient stockholder's gross income. Sections 22(a) and 115(a), Internal Revenue Code of 1939; Sections 61(a) and 316(a), Internal Revenue Code of 1954, *supra*, pp. 2-4. The single question here is whether the withdrawals by petitioner from the family-controlled corporation constituted a loan or a taxable dividend. It is well settled that this issue presents a question of fact. See, *e.g.*, *John Kelley Co.* v. *Commissioner*, 326 U.S. 521; *Regensburg* v. *Commissioner*, 144 F. 2d 41 (C.A. 2), certiorari denied, 323 U.S. 783; *Clark* v. *Commissioner*, 266 F. 2d 698 (C.A. 9); *Niederkrome* v. *Commissioner*, 266 F. 2d 238 (C.A. 9), certiorari denied *sub nom. Royce* v. *Commissioner*, 359 U.S. 945; *Lengsfield* v. *Commissioner*, 241 F. 2d 508 (C.A. 5); *Anketell Lumber & Coal Co.* v. *United States*, 1 F. Supp. 724 (C. Cls.). There is therefore no issue of general importance requiring further review by this Court.

Moreover, the findings that the withdrawals constituted dividends are fully supported by the evidence. The courts below relied on the fact that the withdrawals were continuous and substantial; the absence of notes or collateral for the substantial amounts withdrawn; the absence of an agreement of repayment; the absence of any substantial evidence of any intent or plan on the part of petitioner to repay the withdrawals; the lack of actual repayment before the beginning of the Service's audit (of the only two credits, one was a bookkeeping transaction and the other came after the audit began); and the fact that no dividends were declared or paid, despite the steadily rising earned surplus. In sharp contrast,

when petitioner and his family loaned money to the corporation, it executed notes in favor of the lenders and the loans were repaid, with interest, within approximately six years. Petitioner, on the other hand, relies on his own testimony and that of his brother-in-law, who was also a stockholder; the accounting entries on Towne's books; the fact that the withdrawals were not in proportion to each stockholder's interest in the corporation; and a statement that the withdrawals were loans, made in petitioner's pleadings in a suit brought by United Artists against Towne, its officers, and directors for mismanagement (R. 8–9).[5] As the court below stated, the evidence urged by petitioner "cannot overcome the proper inference that [petitioner] was taking advantage of his position in a closely-held family corporation to provide himself with disguised dividends with nothing more than an accounting entry that such payments were loans and with no obligation to repay" (Pet. 6a).

Petitioner asserts (Pet. 9–21) that an incorrect legal standard was applied to the facts. Citing *North American Oil Consolidated* v. *Burnet*, 286 U.S. 417, 424, and *Commissioner* v. *Wilcox*, 327 U.S. 404, 407–408 (Pet. 9–11), he states that a taxpayer receives taxable income only if he claims the money received as of right and he has no definite, unconditional obliga-

[5] This statement was fully consistent with petitioner's interests in that litigation. For if petitioner had admitted that the withdrawals were dividends, instead of loans, United Artists was entitled to proportionate distributions. Since no such distributions were made, United Artists' allegations of mismanagement would have been strongly supported by the preference of some stockholders over others in paying dividends.

tion to repay. But both courts below specifically held, after detailed consideration of the evidence, that petitioner had no intention or obligation to repay the corporation, and that therefore the withdrawals were not loans (R. 14; Pet. 6a). Thus, the holdings below are fully consistent with the standards laid down by this Court.[6]

CONCLUSION

For the foregoing reasons, we submit that the petition for a writ of certiorari should be denied.

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MAY 1961.

[6] Petitioner also claims (Pet. 28) that the court below did not determine whether the findings were supported by the record The opinion below, however, unmistakably shows that the court reached its conclusion that the payments in question were dividends upon a full consideration of the record, including "all relevant factors indicating the true intent of the parties" (Pet. 6a).

U. S. GOVERNMENT PRINTING OFFICE 1961